

Civil No. 11-2271 (GAG)

1 fraudulent conveyances, and adverse domination, as well as against Chartis and other insurers who
2 provided excess policies to the D&O's for enforcement of such policies.

I. Background

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5 The FDIC intervened in a suit brought in the Puerto Rico Commonwealth Court by W
6 Holding and the D&O's against Chartis for declarations of coverage under liability policies, pursuant
7 to the Puerto Rico Direct Action Statute. (*Id.*, ¶¶ 10, 28.) The FDIC, as Westernbank's receiver,
8 seeks recovery of \$176.02 million in damages from former Westernbank D&O's and their conjugal
9 partnerships¹ for twenty-one allegedly grossly negligent commercial real estate, construction, and
10 asset-based loans and transactions approved and administered from January 28, 2004, through
11 November 19, 2009. (Docket No. 182, ¶¶ 2-3.) The FDIC also requests the court to enforce
12 contracts for liability coverage between the D&O's and Chartis, as well as excess liability policies
13 with XL Speciality Insurance Company ("XL"), Liberty Mutual Insurance Company ("Liberty"), and
14 Ace Insurance Company ("Ace"). (*Id.*, ¶¶ 53-55.) Lastly, the FDIC names Luis Bartoleme Rivera-
15 Cuebas, Carlos Gonzalez-Alonso, and Jane Doe in their capacities as trustees of the Socio Cultural
16 Conservation Trust, the Dominguez Sotomayor Family Trust, and the CT Family Trust, respectively,
17 for administering funds procured through allegedly fraudulent transfers. (*Id.*, ¶¶ 55(A)-55(C).)

18 The FDIC's complaint alleges several acts of purported gross negligence, such as
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21 ¹ The D&O's comprise Frank C. Stipes-Garcia, Juan Carlos Frontera-Garcia, Hector L. Del
22 Rio-Torres, William M. Vidal-Carvajal, Cesar A. Ruiz-Rodriguez, and Pedro R. Dominguez-Zayas.
23 The complaint lays out their respective roles within Westernbank during the timeframe of the alleged
24 grossly negligent behavior. Certain D&O's served on Westernbank's Senior Lending Committee
25 ("SLC") and Senior Credit Committee ("SCC"). The FDIC asserts claims against the following
26 former D&O's, as well: Jose Biaggi-Landron, Ricardo Cortina-Cruz, Miguel A. Vazquez-Seijo, Julia
27 Fuentes del Collado, Mario A. Ramirez-Matos, and Cornelius Tamboer. The conjugal partnerships
joined also include Marlene Cruz-Caballero, Lilliam Diaz-Cabassa, Gladys Barletta-Segarra,
Hannalore Schmidt-Michels, Sonia Sotomayor-Vicenty, the partner of Jose Biaggi-Landron (referred
to as Jane Doe in the complaint), Elizabeth Aldebol de Cortina, Sharon McDowell-Nixon, and Olga
Morales-Perez. (See *id.* ¶¶ 22-52.)

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1 Westernbank’s violations of loan-to-value ratio limits, lack of required borrower equity, inadequate
2 real estate appraisals, insufficient analyses of collateral or inadequate collateral, and insufficient
3 borrower repayment information and repayment sources. (Id., ¶ 5.) The FDIC also asserts that the
4 D&O’s increased, extended, and renewed expired and deteriorating loans to enable continued
5 funding of interest reserves, thereby delaying losses and defaults and increasing the losses on the
6 loans. (Id.)

7 The FDIC claims Westernbank’s officers violated major loan terms by “administering and
8 funding the construction and asset-based loans.” Specifically, the FDIC states that the officers
9 “continued funding asset-based loans despite receipt of reports showing dilution,” violated
10 “borrower covenants and loan agreements,” approved ineligible collateral, engaged in unilateral and
11 unauthorized waiver of key borrower financial covenants relating to working capital, disregarded
12 net adjusted equity value and cash flow ratios, manipulated loan monitoring systems, funded loans
13 despite borrower defaults, and extended expired loans. (Id. at 6.) The FDIC also alleges that the
14 directors “failed to heed and act upon examiner and auditor warnings of deficiencies in commercial
15 lending and administration.” (Id. at 8; see also ¶ 58 (exceeding ratio limits); ¶ 59 (loan approval
16 despite internal admonishment of “severe deficiencies”); ¶¶ 60-63 (detailing alleged disregard of
17 regulator warnings); ¶ 64 (D&O acknowledgment of malfeasance); ¶¶ 69-76 (levying specific
18 allegations against the D&O’s), and; ¶ 84 (summarizing alleged gross negligence).)

19 The FDIC discusses in detail several loans that allegedly led to the \$176.02 million in losses
20 issued to Museum Towers, LP (“Museum Towers”), Yasscar Development Corporation (“Yasscar
21 Development”), Yasscar Caguas Development Corporation (“Yasscar Caguas”), Sabana Del Palmar,
22 Inc. (“Sabana”), Plaza CCD Development Corporation (“Plaza CCD”), Inyx, Inc. (“Inyx”), and
23 Intercoffee, Inc. (“Intercoffee”). The complaint details why and how the loan approvals violated
24 various internal policies, which D&O approved the loan and at what stage the D&O granted approval
25 or administered the financing, and the accountable percentage of the aggregate \$176.02 million loss.
26 (Id., ¶¶ 77-80.)

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1 The FDIC asserts seven claims in its complaint: (1) gross negligence; (2) breach of fiduciary
2 duty against Tamboer; (3) adverse domination; (4)-(6) fraudulent transfers against Stipes, Tamboer,
3 and Dominguez, and; (7) direct action claims against the insurance carriers. (Docket No. 182, ¶¶
4 83–100.) Presently before the court are seven motions to dismiss the FDIC’s complaint filed by the
5 D&O’s and their conjugal partnerships. (Docket Nos. 196, 198, 199, 200, 202, 205, & 291.) For
6 the reasons stated herein, after reviewing the parties’ memoranda of law, submissions, and
7 attachments thereto, the court **DENIES** all motions to dismiss.

II. Motion to Dismiss Standard

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10 “The general rules of pleading require a short and plain statement of the claim showing
11 that the pleader is entitled to relief.” Gargano v. Liberty Intern. Underwriters, Inc., 572 F.3d 45,
12 48 (1st Cir. 2009) (citations omitted) (internal quotation marks omitted). “This short and plain
13 statement need only ‘give the defendant fair notice of what the . . . claim is and the grounds upon
14 which it rests.’” Id. (quoting Bell Atl. Corp. v. Twombly, 550 U.S. 544, 555 (2007)).

15 Under Rule 12(b)(6), a defendant may move to dismiss an action against him for failure
16 to state a claim upon which relief can be granted. See FED. R. CIV. P. 12(b)(6). To survive a
17 Rule 12(b)(6) motion, a complaint must contain sufficient factual matter “to state a claim to
18 relief that is plausible on its face.” Twombly, 550 U.S. at 570. The court must decide whether
19 the complaint alleges enough facts to “raise a right to relief above the speculative level.” Id. at
20 555. In so doing, the court accepts as true all well-pleaded facts and draws all reasonable
21 inferences in the plaintiff’s favor. Parker v. Hurley, 514 F.3d 87, 90 (1st Cir. 2008). However,
22 “the tenet that a court must accept as true all of the allegations contained in a complaint is
23 inapplicable to legal conclusions.” Ashcroft v. Iqbal, 556 U.S. 662, 678 (2009). “Threadbare
24 recitals of the elements of a cause of action, supported by mere conclusory statements, do not
25 suffice.” Id. at 678-79 (quoting Twombly, 550 U.S. at 555). “[W]here the well-pleaded facts do
26 not permit the court to infer more than the mere possibility of misconduct, the complaint has
27 alleged-but it has not ‘show[n]’-‘that the pleader is entitled to relief.’” Iqbal, 556 U.S. at 679

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1 (quoting FED. R. CIV. P. 8(a)(2)).
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3 **III. Discussion**

4 1. Counts 1-3: Gross Negligence, Fiduciary Duty, Delayed Discovery & Adverse
5 Domination

6 The D&Os' motions to dismiss the FDIC's claims for negligence are **DENIED**. (Docket
7 Nos. 196, 198, 199, 200, 202, 205, & 291.) The FDIC must demonstrate the D&O's were grossly
8 negligent, as directors and officers are shielded from ordinary negligence claims under Puerto Rico's
9 Business Judgment Rule.² See W Holding, Inc. v. Chartis Insur. Co., P.R., 845 F. Supp. 2d 422, 429
10 (D.P.R. 2012). To reiterate, the FDIC states sufficient facts to allege a plausible claim for gross
11 negligence, thereby satisfying Twombly and Iqbal. Therefore, any claim arising under ordinary
12 negligence is dismissed. The court considers the allegations and corresponding motions to dismiss
13 in turn.

14 **A. The FDIC's Complaint Sufficiently Alleges Gross Negligence**

15 The Financial Institutions Reform, Recovery, and Enforcement Act ("FIRREA") imposes
16 personal liability on directors or officers of insured depository institutions for gross negligence.

17
18 ² P.R. LAW ANN. 14 § 3563 states,

19
20 The directors and officers shall be bound to dedicate to the affairs of
21 the corporation and to the exercise of their duties the attention and
22 care which in a similar position and under analogous circumstances
23 a responsible and competent director or officer would execute in
24 applying his/her business judgment in good faith or his/her best
25 judgment in the case of nonprofit corporations. Only gross
26 negligence in the exercise of the duties and obligations mentioned
27 above shall result in personal liability (emphasis added).

28 The statute does not distinguish between directors and officers in imposing a gross
negligence threshold for liability. Therefore, the court assesses directors and officers equally.

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1 Section 1821(k) of FIRREA provides that the definition of gross negligence should be grounded in
2 state law. Puerto Rico models its corporate statutes after Delaware corporate law. See Wylie v.
3 Stipes, 797 F. Supp. 2d 183, 196 (D.P.R. 2012) (citing Marquis Theatre Corp. v. Condado Mini
4 Cinema, 846 F.2d 86, 91 (1st Cir. 1988)). Gross negligence constitutes a difficult threshold to reach.
5 In assessing gross negligence claims, a reviewing court looks “for evidence as to whether a board
6 has acted in a deliberate and knowledgeable way in identifying and exploring alternatives.” Citron
7 v. Fairchild Camera & Instrument Corp., 569 A.2d 53, 66 (Del. 1989). Gross negligence “involves
8 a devil-may-care attitude or indifference to duty amounting to recklessness.” Zimmerman v.
9 Crothall, 2012 Del. Ch. LEXIS 64, at *20 (Del. Ch. Mar. 5, 2012) (citing In re Lear Corp.
10 Shareholder Litig., 2005 Del. Ch. LEXIS 133, 2005 WL 2130607, at *4 (Del. Ch. Aug. 26, 2005)).
11 Gross negligence constitutes “reckless indifference or actions that are without the bounds of reason.”
12 McPadden v. Sidhu, 964 A.2d 1262, 1274 (Del. Ch. 2008). The “intentional dereliction of a known
13 duty,” furthermore, “is a higher standard of wrongdoing than gross negligence or recklessness.” In
14 re Walt Disney Co. Deriv. Litig., 906 A.2d 27, 67 (Del. Ch. 2005).

15 Parallel FDIC actions against various directors and officers guide the court in its analysis.
16 Although FIRREA dictates that state-based gross negligence doctrine governs claims against
17 directors and officers, and the facts of each case differ, these cases nonetheless assist the court. See
18 e.g., FDIC v. Briscoe, No. 11-CV-2303 (N.D. Ga. Aug. 14, 2012); FDIC v. Willetts, No. 7:11-DV-
19 165, 2012 U.S. Dist. LEXIS 55363 (E.D.N.C. Apr. 13, 2012); FDIC v. Skow, No. 11-111 (N.D. Ga.
20 Feb. 27, 2012); FDIC v. Spangler, No. 10-CV-4288 (N.D. Ill. Dec. 22, 2011); FDIC v. Saphir, No.
21 10-7009 (N.D. Ill. Sept. 1, 2011).

22 In Briscoe, the FDIC alleged violations of law and regulations; failure to establish, enforce,
23 and follow loan policies; inadequate investigation; failure to heed regulatory warnings; loans to non-
24 creditworthy borrowers; inadequate financial information; inadequate loan documentation; unsecured
25 and undersecured loans; inadequate or non-existent appraisals; failure to perfect and maintain
26 collateral; diversion of loan proceeds; improper loan repayment programs; improper loan extensions
27 and renewals; inadequate collection procedures; improper selection and supervision of officers;

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1 improper investment and liquidity policy compliance; improper maintenance of capital-to-asset ratio;
2 insider loans; and failure to properly exercise management and supervision duties. See slip op. at
3 12-13. The court found that the complaint alleged sufficient facts for gross negligence and requested
4 the FDIC to replead sufficient facts as to each specific D&O in the group. Id. at 16, 19.

5 In Spangler, the FDIC alleged that “Loan Committee Defendants failed to follow the bank’s
6 written lending policies and ensure prudent underwriting in approving the ‘Loss Loans.’ The Loan
7 Committee allegedly approved loans without current and complete financial information on the
8 borrower and guarantor and without obtaining a full guarantee on the loans.” See slip op. at 4-5.
9 The FDIC also alleged failure to assess repayment abilities of borrowers and creditworthiness before
10 allowing generous interest reserves, as well as funding loans that were not financially feasible, failure
11 to address repeated regulatory warnings about the state of the bank, and breach of commitments to
12 regulators that the bank would limit total loans. Id. at 5, 10. The court recognized Illinois’s gross
13 negligence standard as “very great negligence,” rejecting a “recklessness definition.” Id. at 8.

14 In denying the motion to dismiss, the court noted, “[I]t is not clear that Defendants’ action
15 can be chalked up to ‘a recession.’ While it is too early in the case to know whether the evidence
16 will show that Defendants too were victims of the recession, the amended complaint does not
17 attempt to hold the Loan Committee Defendants accountable for failing to foresee future economic
18 developments.” Id. at 11. The Spangler court considered vagueness claims, noting that the
19 defendants claimed the allegations were “nothing but vague assertions that officers and directors did
20 not conform to a loan policy or get a personal guarantee.” Id. at 12. The court found this argument
21 unconvincing, ruling that the FDIC met the gross negligence standard.

22 In Saphir, Judge Pallmeyer found sufficient pleadings for gross negligence for alleged failure
23 to adequately implement and supervise loan programs, voting to approve the allegedly toxic loans,
24 failing to increase the bank’s reserves, and approving large dividend and incentive payments that
25 depleted the bank’s capital. See slip op. at 10. The court was not “troubled by the FDIC’s purported
26 failure to say ‘how’ or ‘why’ the Defendants’ conduct deviated from the applicable standard of care,
27 or to attach [the bank’s] charter . . .” Id. at 12.

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1 In Skow, the court found sufficient allegations of gross negligence where the FDIC asserted
2 that the directors and officers “deliberately pursued a speculative, high-growth lending strategy, the
3 risks of which were compounded by their failure to implement sound lending practices or to exercise
4 appropriate oversight over loan officers and the lending function,” and failed to heed regulator
5 warnings. See slip op. at 12-13.

6 Lastly, in Willetts, the court denied the defendants’ 12(b)(6) motion where the FDIC alleged
7 that “directors were repeatedly warned about regulator violations and were advised that loans were
8 being made in violation of the loan policy but took no action.” See 2012 U.S. Dist. LEXIS 55363,
9 at *12. The FDIC also contended that “many loans were approved after an inappropriate level of
10 review,” and that the bank was improperly structured, lacked feasibility studies, overstated value,
11 and lacked sufficient appraisal bases. Id. at *12-13.

12 In the instant case, the FDIC alleges “funding of loans in the face of repeated borrower
13 defaults, ineligible collateral, cash diversions, and violations of fundamental loan terms and
14 covenants in order to continue to collect interest and derive short term profits,” “failure to obtain
15 appraisals . . . in violation of bank policy . . .,” “failure to require compliance with loan to value ratio
16 limits as required by bank policy,” “failure to disclose personal interests in a loan or borrower, and
17 self dealing [sic],” and failure to “heed and act upon escalating examiner and auditor warnings of
18 deficiencies in commercial lending and administration.” (See Docket No. 233 at 2-3) (citing Docket
19 No. 182 at ¶¶ 4, 56, 57, 80(D), 84; 5, 58, 77, 80(A), (B), (F), (G), and (H); 5, 58, 77, 80(A), (F), (G),
20 and (H); 5, 77, 80(C)-(E); 7, 80(F), 82; 8, 60-63, 68, 69, & 84, respectively); see also Docket No.
21 182, ¶¶ 66-67, 79, 80(d) (sufficiently alleging breach of banking procedure against Ruiz). The
22 similarities between the allegations against the Westernbank D&O’s and those in Illinois, North
23 Carolina, and Georgia are overwhelmingly evident. The FDIC’s allegations exceed the requirements
24 set forth in Iqbal and Twombly.

25 A critical distinction between the Delaware and Illinois-Georgia-North Carolina standards
26 for gross negligence lies in Delaware’s strict definition and merits mention. Where some states find
27 gross negligence does not quite encompass recklessness, Delaware embraces it. Reckless

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1 indifference outside the bounds of reason and a devil-may-care attitude certainly necessitate proffers
2 of egregiousness beyond those required in other jurisdictions recognizing gross negligence.
3 Nonetheless, the FDIC alleges facts questioning “whether a board has acted in a deliberate and
4 knowledgeable way in identifying and exploring alternatives” analogous to those encountered by our
5 sister courts in denying their respective motions to dismiss. See Citron v. Fairchild Camera &
6 Instrument Corp., 569 A.2d 53, 66 (Del. 1989). The FDIC supplements its bottom-line allegation
7 of a grossly negligent loss of \$176 million with over 90 pages of fact and law that unquestionably
8 put the defendants on notice of exactly that which they are accused. Furthermore, the motions to
9 dismiss do not specifically address Tamboer’s alleged breach of fiduciary duty beyond their
10 objections to the FDIC’s claims for gross negligence; thus, nor shall the court.

11 Lastly, the D&O’s in both this and several other FDIC-D&O cases argue that vagueness in
12 the complaint precludes individual directors and officers from understanding with certainty for which
13 actions the FDIC holds them accountable. Indeed, the Briscoe court required the FDIC to amend its
14 complaint to specify which allegedly negligent actions were attributed to which director or officer.
15 See slip op. at 19. Here, however, the FDIC explicitly chronicles which director or officer approved
16 which purportedly grossly negligent loan, when the approval occurred, whether the loan constituted
17 an initial loan, additional credit, extension of construction loan, or post-approval administration and
18 funding. (See Docket No. 182, ¶ 79.) The FDIC subsequently discusses in extensive detail the
19 various pitfalls in the D&Os’ approval of the loans. (Id. at ¶ 80.) The FDIC’s memorandum
20 opposing the various motions to dismiss delves further into specific allegations of wrongdoing and
21 need not be recited here. (See Docket No. 233 at 9-16.) Several of the D&O’s have also filed
22 individual motions to dismiss. Although these motions adopt by incorporation the D&O’s motion
23 discussed above, they raise separate concerns that the court considers below and ultimately **DENIES**.

24
25 i. Insurers on behalf of D&O’s & Conjugal Partnerships [196]

26 The claims set forth in this motion to dismiss are addressed in count 7.

Civil No. 11-2271 (GAG)ii. Stipes, Frontera, Del Rio, Vidal, Ruiz, & Dominguez [198]

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2 This motion alleges issue preclusion pursuant to this court's decision in Wylie v. Stipes, 797
3 F. Supp. 2d 193, 194 (D.P.R. 2011). Issue preclusion "forecloses relitigation in a subsequent action
4 of a fact essential for rendering a judgment in a prior action . . . , even when different causes of action
5 are involved." Gener-Villar v. Adcom Group, Inc., 417 F.3d 201, 205-06 (1st Cir. 2005). The
6 D&O's argue the Wylie plaintiffs brought derivative claims for breaches of fiduciary duties based
7 on allegedly negligent failure to implement adequate internal controls at Westernbank, the issue of
8 negligence was essential to judgment, and the court dismissed the action on summary judgment.
9 (See Docket No. 198 at 34-35.)

10 This allegation lacks merit. Wylie brought a shareholder derivative suit against certain
11 D&O's of W Holding for alleged Sarbanes-Oxley violations, breach of fiduciary duties, waste of
12 corporate assets, unjust enrichment, and violations of the Puerto Rico General Corporations Law of
13 1995. 797 F. Supp. 2d at 194. The court considered the appropriateness of a Special Litigation
14 Commission's determination to quash the derivative suit. The court analyzed the SLC members'
15 ability to independently assess plaintiff's claims, allegations of improper delegation, the
16 thoroughness of the SLC's investigation, and the reasonableness of the SLC's findings. Id. at 200-
17 205. To the extent the D&O's consider granting summary judgment on the "reasonableness of the
18 SLC's findings" preclusive, the standard bears repeating to dispel such a notion. The court
19 determined whether "the report of the committee appears to be comprehensive and well documented
20 and gives indication of a reasonable and thorough investigation of the plaintiff's allegations." Id.
21 at 201. The court issued no judgment as to the D&O's purported negligence, let alone mentioned
22 the word "negligence" once; rather, it listed the various factors to consider in assessing the
23 reasonableness of the SLC's recommendation, which included whether the directors should have
24 known that violations of law were occurring and took no steps in good faith to prevent the breach.
25 Id. at 202. For estoppel purposes, the relevant issue the court decided in Wylie is whether the SLC
26 presented reasonable recommendations based on certain criteria used to determine if the SLC could
27 plausibly find a lack of oversight. Finding reasonableness in the recommendation does not entail

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1 a final decision on whether the D&O's engaged in reckless behavior with a devil-may-care attitude
2 resulting in \$176 million in losses. Consequently, the court rejects this argument.

3 iii. Barletta, Schmidt, Sotomayor, Diaz, & Cruz [199] and McDowell [205]

4 The conjugal partners of the D&O's assert that claims against them should be dismissed
5 because they are not liable under FIRREA or Puerto Rico law. To reiterate, FIRREA adopts state
6 law standards. Therefore, the court need only assess whether the claims against the conjugal
7 partnerships plausibly entitle the FDIC to relief according to Puerto Rico law.

8 This motion to dismiss first asserts the spouses cannot be subjected to personal liability.
9 (Docket No. 199 at 2.) The FDIC clarifies it "does not assert any individual liability of the spouses
10 beyond their interests in the conjugal partnerships." (See Docket No. 233 at 25) (citing Docket No.
11 182, ¶ 28.) Therefore, the only questions remaining concern the conjugal partnerships' liability.
12 The movants claim the partnerships' liability for acts of one spouse is subsidiary under Puerto Rico
13 law and the court should exclude them from the present action until adverse judgment against the
14 D&O's. Each spouse, as an individual, is not responsible for all the obligations of the conjugal
15 partnership. However, when a spouse's negligent conduct generates economic benefits for the
16 partnership, the partnership is liable for the resulting damages. See Lugo Montalvo v. González
17 Mañón, 104 D.P.R. 372, 378 (P.R. 1975); Sepúlveda v Maldonado, 108 D.P.R. 530, 534 (P.R. 1979).
18 The conjugal partnership will not be liable when no economic benefit for the partnership exists,
19 when the spouse was involved in an illegal act that constitutes a crime of intention, and when the
20 damages are caused by a spouse while acting as a public employee performing official duties, such
21 as a violation of civil rights or sexual harassment. See generally Rosario v. Distribuidora Kikuet,
22 Inc., 151 D.P.R. 634, 648 (P.R. 2000). Here, the complaint and reply name the partnerships, placing
23 them on notice that elements of the partnerships may have engaged in a course of negligent conduct
24 exposing them to liability. Therefore, the partnerships are properly included.

25 iv. Fuentes [200], Biaggi [202], and Aldebol [291]

26 The court addresses these issues in Part A and Part B of this Section.

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B. Statutes of Limitation and Adverse Domination

Preliminarily, the court observes that the FDIC timely files this suit under FIRREA. The FDIC's statute of limitations for any action in tort is the longer of the three-year period beginning on the date the claim accrues; or the period applicable under State law. See 12. U.S.C. § 1821 (d)(14)(A)(ii). The FDIC assumed receivership of Westernbank on April 30, 2010. Therefore, no question exists as to whether the FDIC timely files this suit under its federal limitations period.

i. Statute of Limitations

The D&O's assert that a one-year statute of limitations bars negligence claims of the allegedly negligent loans and that codification of the Business Judgment Rule limitations period should not apply because it does not constitute "liability created by law." These arguments are inapposite. Actions against directors or stockholders enjoy a three-year statute of limitations.³ Liability created by statute seemingly constitutes a liability created by law. See Platt v. Wilmot, 193 U.S. 602, 613 (1904) (finding that contract liability arising under statute constitutes "liability created by statute.") Distinguishing "liability created by statute" from "liability created by law," which applies to the Puerto Rico statute at issue here, offends common sense. Legislatures create new laws or create new statutes by codifying common law. The court understands that "at law" invokes the common law; however, in this instance, the Puerto Rico legislature codified a common law principle. It appears, thus, that the Business Judgment Rule in Puerto Rico falls under the auspices of both common law and statutory law. Either way, the liability at issue here arose under law. Plaintiff-Officers also contend that the statute encompasses only directors and not officers. Indeed, the wording only references directors and stockholders. The court reserves judgment on this issue, as the officers are nonetheless amenable to suit for gross negligence because adverse domination and delayed discovery rules toll the limitations period.

³ Actions against directors or stockholders of corporations must be brought within three years after the discovery by the aggrieved party of the facts upon which the penalty or forfeiture attached or the liability was created. See P.R. LAWS ANN. 32 § 261.

Civil No. 11-2271 (GAG)ii. Adverse Domination & Delayed Discovery

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2 Adverse domination is “an equitable doctrine which operates to toll the statute of limitations
3 for a corporation’s claims against its officers or directors when the persons in charge of the
4 corporation cannot be expected to pursue claims adverse to their own interests.” In re Payroll
5 Express Corp., 186 F.3d 196, 205 (2nd Cir. 1999). This court decided the seminal case on adverse
6 domination in FDIC v. Bird, 516 F. Supp. 647 (D.P.R. 1981). In Bird, the district court crafted the
7 principle the court follows today: “Control of the association by culpable directors and officers
8 precludes the possibility of filing suit because these individuals can hardly be expected to sue
9 themselves or to ‘initiate any action contrary to their own interests.’” FSLIC v. Williams, 599 F.
10 Supp. 1184, 1194 (D. Md.) (quoting Bird, 516 F. Supp. at 652). Several courts adopt this rationale
11 and cite Bird to justify their decisions. See e.g., FDIC v. Manatt, 723 F. Supp. 99, 105 (E.D. Ark.
12 1989); FDIC v. Appling, 992 F.2d 1109, 1115 (10th Cir. 1993); FDIC v. Paul, 735 F. Supp. 375,
13 377-78 (1990); Resolution Trust Corp. v. Fiala, 870 F. Supp 962, 972-73 (E.D. Mo. 1990) (citing
14 cases).

15 The Supreme Court has squarely rejected developing federal common law to govern the
16 standard of care used to measure the legal propriety of the conduct of directors, holding instead that
17 state common law principles govern liability in tort. See Atherton v. FDIC, 519 U.S. 213, 217-26
18 (1997); see also O’Melveny & Myers v. FDIC, 512 U.S. 79, 89 (1994). In O’Melveny & Myers, the
19 Court rebuffed the “runaway tendencies of ‘federal common law’ untethered to a genuinely
20 identifiable (as opposed to a judicially constructed)” law, finding that “extraordinary cases” warrant
21 judicial creation of a federal rule. 512 U.S. at 89. While the FDIC alleges gross negligence pursuant
22 to P.R.LAWS ANN. 14 § 3563 rather than common law tort, negligence principles sound in both and,
23 therefore, merit consideration of whether Bird’s rationale constitutes federal common law or state
24 common law. The answer is that the original opinion created federal common law prior to the
25 Court’s holding in O’Melveny & Myers. But Puerto Rico jurisprudence tolling statutes of limitation
26 for delayed discovery sufficiently embraces the principles espoused in Bird. The First Circuit
27 recognizes that Puerto Rico adheres to this rationale, holding that a statute of limitations “does not

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1 begin to run until the plaintiff possesses, or with due diligence would possess, information sufficient
2 to permit suit.” Villarini-Garcia v. Hosp. Del Maestro, 8 F.3d 81, 84 (1st Cir.1993) (citing Santiago
3 Hodge v. Parke Davis & Co., 909 F.2d 628, 632-33 (1st Cir.1993) (discussing Colon Prieto v.
4 Geigel, 115 P.R. 232, 247 (P.R. 1984))).

5 The D&O’s also argue that adverse domination should only apply to claims sounding in
6 fraud; however, the Bird court weighed negligence claims in implementing adverse domination.
7 Distinguishing negligence from fraud here would defeat the core purpose of the doctrine. Regardless
8 of the D&Os’ intent, if putative plaintiffs are not situated to become aware of egregious lending
9 practices and the corporation neglects to sue the directors and officers, a harm arises necessitating
10 tolling. To toll the statute on the ground of adverse domination, “at least once the facts giving rise
11 to . . . liability are known, plaintiff must effectively negate the possibility that an informed
12 stockholder or director could have induced the corporation to sue.” Int’l Inv. Trust v. Cornfeld, 619
13 F.2d 909, 930 (2nd Cir. 1980) (quoting Int’l Ry. of Cent. Am. v. United Fruit Co., 373 F.2d 408,
14 412-17 (2nd Cir. 1967)). Although the D&O’s expressly reject the principle of adverse domination,
15 the complaint states and the D&O’s acknowledge that the restated Form 10-K filed by the W
16 Holding Board on March 16, 2009, placed any putative plaintiffs on notice of ostensibly grossly
17 negligent action. The FDIC’s reference to Form 10-K and the D&O’s acknowledgment that the form
18 disclosed potential dereliction of duty sufficiently raises the right to relief above a speculative level.

19 Adverse domination and lack of disclosure toll the limitations period for any grossly
20 negligent actor, whether or not employed by Westernbank when it published the Form 10-K or when
21 the FDIC assumed receivership. Thus, Fuentes and Biaggi are not exempt. Excluding D&O’s under
22 this rationale would reward grossly negligent actors who simply foresee potential litigation and
23 resign. Following discovery, the D&O’s may proffer evidence revealing practices discoverable prior
24 to the Form 10-K filing on March 16, 2009 not obfuscated by adverse domination, so as to start
25 running the three-year clock at an earlier date.

26
27 2. Counts 4-6: Fraudulent Conveyance – Stipes, Tamboer, and Dominguez

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1 The court **DENIES** motions to dismiss regarding fraudulent conveyances attributed to Stipes
2 and Dominguez.⁴ The FDIC may avoid a transfer of any interest of an institution-affiliated party,
3 or any person who the FDIC determines is a debtor of the institution if such party or person made
4 such transfer or incurred such liability with the intent to hinder, delay, or defraud the insured
5 depository institution or the FDIC. See 12 U.S.C. § 1821(d)(17). The statute requires: 1) the
6 fraudulent transferor be an institution-affiliated party or debtor, and; 2) the transferor performs the
7 transfer with the intent to hinder, delay, or defraud Westernbank or the FDIC. Stipes and Dominguez
8 assert that the FDIC fails to establish either prong.

9 The D&O's contest whether the FDIC appropriately categorizes Stipes and Dominguez as
10 debtors or institution-affiliated parties, calling to question the FDIC's interpretation of 12 U.S.C. §
11 1821(d)(17). Stipes and Dominguez comprise institution-affiliated parties because they were
12 directors and officers of the institution during the purportedly negligent actions for which the FDIC
13 seeks damages. The D&O's argue that because they were not affiliated at the time of conveyance,
14 the statute does not apply to them. However, the court finds RTC v. Greif persuasive. 906 F. Supp.
15 1457, 1465 (D. Kan. 1995) (finding statutory authority under Section 1821(d)(17) to determine that
16 former directors and officers are institution-affiliated parties). Holding otherwise would permit the
17 D&O's to shield themselves from liability simply by resigning.

18 The question thus becomes one of concurrence – whether the FDIC may simultaneously
19 allege fraudulent conveyance without a judgment against the D&O's. The court finds such action
20 permissible under the federal scheme, but questions of ripeness arise for allegations under state law.
21 Sucesion Almazan v. Lopez holds that a petitioner must be “really and truly a lawful creditor of
22 defendants.” 20 P.R.R. 502, 506 (P.R. 1914). Section 1821(d)(17), furthermore, permits the FDIC
23 to determine who “is a debtor of the institution.” While this provision hardly bestows omnipotence
24 on the FDIC to simply label the D&O's “debtors,” claims for arbitrary and capricious interpretation

25
26 ⁴ The D&Os' do not address Tamboer's alleged fraudulent conveyance; thus, neither shall
27 the court.

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1 are more appropriate at the summary judgment stage. In any case, the Lopez court found that if
2 plaintiffs obtain judgment during the course of an action for rescission, “this would be a
3 circumstance in corroboration of the right of the plaintiff.” Id. If the trier of fact finds the D&O’s
4 liable for gross negligence, the FDIC justifiably dubs Stipes and Dominguez debtors. In contrast,
5 the fraudulent conveyance claims necessarily falter if the FDIC fails to sufficiently demonstrate gross
6 negligence. Therefore, the FDIC satisfies the first prong of Section 1821(d)(17).

7 Secondly, the FDIC must allege an intent to hinder, defraud, or delay. The First Circuit
8 recognizes that courts often find fraudulent conveyances through circumstantial evidence. See e.g.,
9 Max Sugarman Funeral Home, Inc. v. A.D.B. Investors, 926 F.2d 1248, 1254 (1st Cir.1991). At this
10 stage, the court finds the allegations of badges of fraud in the complaint sufficient to make out a
11 claim for an intent to defraud, hinder, or delay, particularly because Stipes is the primary beneficiary
12 of the trust into which he completed the allegedly fraudulent transfer. (See Docket No. 182 at 30-
13 33.) Discovery is necessary to clarify these questions; thus, the D&O’s motion to dismiss is

14 **DENIED.**

15
16 3. Count 7: Insurers’ Motions to Dismiss

17 Chartis, ACE, XL Speciality, and Liberty (collectively “Insurers”) move to dismiss the
18 FDIC’s claims against them for enforcement of the D&Os’ liability insurance policies, and Chartis
19 moves to dismiss the D&O’s claims against it for enforcement of the D&Os’ liability insurance
20 policies. (Docket No. 197.) The court **DENIES** both motions.

21 The Insurers claim the Insured v. Insured Exclusion⁵ precludes the FDIC from bringing suit
22 to recover on the D&Os’ policies. The Seventh Circuit succinctly describes the Exclusion.
23 “Director and officer liability insurance policies commonly feature so-called insured vs. insured
24 exclusions that exclude from coverage losses for claims brought by one ‘insured’ against another

25 ⁵ The Exclusion in Section 4(i) of the Chartis-D&O Policy reads, “The Insurer shall not be
26 liable to make any payment for Loss in connection with any Claim made against an Insured : . .
27 .which is brought by, on behalf of or in the right of, an Organization or any Insured Person other than
28 an Employee of an Organization, in any respect and whether or not collusive.” (Docket No. 197-4
at 9.)

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1 'insured,'" which includes "current and former [D&O's] as well as the corporation itself . . . to limit
2 moral hazard. Without such an exclusion, a D&O policy could require the insurer to pay for the
3 business mistakes of insured directors and officers if the corporation . . . or if former officers or
4 directors brought suit . . ." Miller v. St. Paul Mercury Ins. Co., 683 F.3d 871, 872 (7th Cir. 2012).

5 Where a regulatory agency asserts claims against insured directors and officers on behalf of
6 both the insured organization and third-party interests, the applicability of the Exclusion is
7 ambiguous. Fed. Ins. Co. v. Hawaiian Elec. Indus. Inc., No. 94-00125, 1995 WL 1916123, 7 (D.
8 Haw. Dec. 15, 1995). "A majority of better-reasoned opinions holds that the 'insured v. insured'
9 exclusion does not unambiguously exclude suits by the FDIC from coverage." Peter D. Rosenthal,
10 Have Bank Regulators Been Missing the Forest for the Public Policy Tree? The Case for Contract-
11 Based Arguments in the Litigation of Regulatory Exclusions in Director and Officer Liability
12 Policies, 75 B.U.L. REV. 155, 173 (1995). Several cases support this notion. See e.g., FDIC v. Am.
13 Cas. Co. of Reading, 814 F. Supp. 1021, 1026 (D. Wyo. 1991) ("Finally, the Court is not convinced
14 that the FDIC, acting as receiver, is in the same position as the institution. While the FDIC steps into
15 the shoes of the predecessor bank, it is nonetheless in the unique position of representing the interests
16 of itself, shareholders, and all other creditors.") (citations omitted); FDIC v. Zaborac, 773 F. Supp.
17 137, 144 (C.D. Ill. 1991) ("In this case, the FDIC does not merely stand in the shoes of [the bank],
18 it can also stand in the shoes of the shareholders; therefore, as a shareholder, it has the independent
19 authority to bring a suit against American Casualty."); Branning v. CNA Ins. Cos., 721 F. Supp.
20 1180, 1184 (W.D. Wash. 1989) ("The court finds, however, that [the] FSLIC does not merely stand
21 in the shoes of Home Savings. By statute, [the] FSLIC represents depositors, shareholders, creditors
22 and the federal insurance fund as well as the failed institution."); Am. Cas. Co. of Reading v. FSLIC,
23 704 F. Supp. 898, 901 (E.D. Ark. 1989) ("Moreover, because the FSLIC is required to marshal the
24 assets of a failed institution for the benefit of its depositors and creditors and to minimize payouts
25 from the insurance fund, it is motivated to bring suit by interests distinctly different from that of an
26 institution which has remained solvent.").

27 However, the Insurers maintain the appropriate course of action requires applying the

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1 Exclusion to FDIC claims. See Hyde v. Fidelity & Deposit Co., 23 F. Supp. 2d 630, 634 (D. Md.
2 1998); see also Mt. Hawley Ins. Co. v. FSLIC, 695 F. Supp. 469, 484 (C.D. Cal. 1987); Powell v.
3 Am. Cas. Co. of Reading, 772 F. Supp. 1188, 1191 (W.D. Okla. 1991) (holding that the “insured vs.
4 insured” exclusion applies to actions brought by the FDIC “which stands in the shoes of the . . .
5 [b]ank in prosecuting claims.”). The Insurers assert that the FDIC stands directly in Westernbank’s
6 shoes and should therefore be precluded from bringing suit under the Exclusion. See also Fid. &
7 Deposit Co. of Md. v. Conner, 973 F.2d 1236, 1240 (5th Cir. 1992) (holding that an “insured vs.
8 insured” exclusion applied to the FDIC when the complaint filed by the FDIC made “no attempt to
9 show an independent breach of duty towards the bank’s depositors or shareholders.”).

10 With these differences in mind, the court turns to the purpose of the Exclusion, the
11 complaint, and the specific terms in the policy for guidance. The obvious intent behind the
12 Exclusion is to protect insurance companies from collusive suits among insured parties. See Michael
13 D. Sousa, Making Sense of the Bramble-Filled Thicket: the “Insured v. Insured” Exclusion in the
14 Bankruptcy Context, 23 BANK. DEV. J. 365, 391 (2007) (citing Fid. & Dep. Co. of Md. v. Zandstra,
15 756 F. Supp. 429, 431 (N.D. Cal. 1990)). Here, the FDIC reaps no benefits comparable to those
16 enjoyed by collusive actors who seek to swindle insurance companies.

17 The policy, however, encompasses claims “brought by, on behalf of or in the right of, an
18 Organization or any Insured Person, . . . whether or not collusive.” (See Docket No. 197 at
19 9) (emphasis added). The court must assess whether FDIC brings suit on behalf of or in the right
20 of an “Organization,” as defined in the policy. The policy defines “Organization” as the named
21 entity, each subsidiary, and debtors in bankruptcy proceedings. (See Docket No. 197-4
22 at 7-8.) Accordingly, the court finds that the FDIC’s course of conduct does not run afoul of this
23 provision and adopts the rationale espoused in Branning and Am. Cas. Co. of Reading v. FSLIC that
24 the Exclusion does not preclude the FDIC from seeking redress from the Insurers.
25

26 The FDIC establishes in its complaint that it “succeeds to the rights, claims, titles, powers,
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28

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1 privileges, and assets of Westernbank and its stockholders, members, account holders, depositors,
2 officers, or directors . . .” (Docket No. 182 at ¶ 21.) The Exclusion and relevant terms in the
3 policy therefore preclude suit on behalf of the members, officers, and directors. The Exclusion also
4 ostensibly prevents the FDIC from bringing suit on behalf of Westernbank’s shareholders, who
5 consist only of W Holding, a plaintiff to this case. Entertaining such a claim would contradict the
6 purpose of the Exclusion by cloaking collusion in an FDIC action. Nonetheless, the FDIC mollifies
7 these concerns by suing on behalf of depositors, account holders, and a depleted insurance fund.
8 The FDIC’s role as a regulator sufficiently distinguishes it from those whom the parties intended to
9 prevent from bringing claims under the Exclusion. Therefore, the Insurers’ motion to dismiss
10 FDIC’s claims is **DENIED**.

11 **IV. Conclusion**

12 For the abovementioned reasons, the court **DENIES** all motions to dismiss [196, 198,
13 199, 200, 202, 205, 291].
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18 **SO ORDERED.**

19 In San Juan, Puerto Rico this 23rd day of October 2012.
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21

/S/ Gustavo A. Gelpí

GUSTAVO A. GELPI

United States District Judge
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